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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1992

BARCLAYS BANK PLC
Petitioner,

VS.

FRANCHISE TAX BOARD,
An Agency of the State of California
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF CALIFORNIA

PETITIONER'S REPLY BRIEF

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INTRODUCTION

Respondent does not deny, nor can it, that this case is of major national and international importance. The United States, the United Kingdom, the United States' major trading partners and all other amici assert that California's application of worldwide combined reporting to foreign taxpayers and to their domestic subsidiaries (i) is at odds with accepted international practice, (ii) has created serious tensions in the United States' conduct of its foreign commercial relations, (iii) has led to threats and enactment of retaliatory legislation and (iv) has seriously undermined the federal government's ability to "speak with one voice when regulating commercial relations with foreign governments." The United States bluntly concludes:

> This Court's resolution of the question presented in this case is of great importance because the analysis applied by the

> California Supreme Court threatens broad impact on the constitutional allocation of authority to the federal government to regulate foreign commerce.

United States Amicus Brief at 15-16.

Further, Respondent does not deny, nor can it, that this case squarely presents the issue which this Court twice reserved in *Container Corp. of America v. Franchise Tax Board,* 463 U.S. 159, 189 n. 26, 195 n. 32 (1983), or that this case contains all of the elements which this Court emphasized as missing in *Container.* Respondent does not deny, nor can it, that the California Supreme Court found affirmative congressional policy where this Court in *Container* found no policy—affirmative or negative —reviewing the same facts. Respondent does not deny, nor can it, that worldwide combined reporting as applied here burdens foreign commerce.[1]

Respondent never addresses the conflict between the decision of the California Supreme Court and this Court's oft-confirmed requirement—both before and after *Wardair Canada v. Florida Department of Revenue,* 477 U.S. 1 (1986)[2] —that congressional consent to remove a state tax from the scrutiny of the commerce clause must be specific, unambiguous and based on an affirmative text. Respondent does not point to that text—nor can it.

Respondent's only response is that all of this is irrelevant because the decision of the California Supreme Court is right. If, as the decision below states, this Court in its *Wardair* decision, a case legally and factually distinguishable from this case, has "reoriented" foreign commerce clause jurisprudence from a consideration of sensitive matters of national sovereignty and foreign relations to a search for the meaning of congressional silence, this Court should say so. If the California court can construct a new test, under which it refuses to follow the analysis of this Court in *Container* on the very question reserved, this Court, not the

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[1] Respondent essentially admits that worldwide combined reporting "has a direct impact upon foreign relations" and "may well adversely affect the power of the central government to deal with foreign affairs issues." Respondent's Brief in Opposition (hereafter "R.B."), at 27.

[2] See *Wyoming v. Oklahoma,* ____ U.S. ____, 112 S. Ct. 789 (1992), which Respondent never mentions.

California Supreme Court, must say that it has overruled *Container* and that the new test is proper.[3] Until then, whether the court below is "right" or not is truly irrelevant.

The balance of Respondent's response rests on the proposition that the California decision does not constitute a final judgment under 28 U.S.C. § 1257. Although Respondent refers to this decision as "interlocutory," the decision represents the final precedential judgment of the highest court in California on these important foreign commerce issues. The subsequent proceedings on the separate due process issue, whatever the outcome, will not affect, or be affected by, that judgment. This Court has recognized that finality is a practical concern which balances the risks of delay in review against the possible costs of piecemeal review. Petitioner has already languished for eight years in the California courts. No purpose is served by further delay. Where, as here, the decision of the court below, separable from and unaffected by the subsequent state proceedings, is eroding basic constitutional policies of uniformity under the dormant foreign commerce clause and undermining the Constitution's allocation of foreign policy matters to the central government, the balance clearly swings to immediate review.

ARGUMENT

I

THIS COURT HAS JURISDICTION OVER THE FINAL DECISION OF THE COURT BELOW ON THE IMPORTANT FOREIGN COMMERCE ISSUES

Respondent argues that the remand of a separate federal question[4] (the due process issue) which cannot affect the foreign commerce issues now finally decided by the California Supreme Court makes that decision insufficiently "final" for purposes of

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[3] This Court frowns on overruling "sub silentio" and it is for this Court, not a lower court, to overrule its decisions. *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 484 (1989).

[4] Respondent suggests that the Court of Appeal might not even reach the remanded issue because Respondent intends to raise state procedural bars. R.B. at 13. If so, the second federal question disappears.

this Court's jurisdiction under 28 U.S.C. § 1257. Respondent's principal contention is that this Court's tests for finality where there are further state court proceedings, as summarized in *Cox Broadcasting Corporation v. Cohn,* 420 U.S. 469 (1975), bar finality whenever such further state proceedings involve a federal question.

There is no such bar. As this Court has stated many times, the question of finality is a practical one. *See, e.g., Cohen v. Beneficial Indus. Loan Corp.,* 337 U.S. 541, 546 (1949). This Court balances competing policy concerns arising from piecemeal review against the dangers and possible waste of delaying justice. This Court's tests include the presence of a second federal question in that balancing process. *Cox,* 420 U.S. 469; *Flynt v. Ohio,* 451 U.S. 619 (1981). The basic policy question is still whether immediate review better serves the identified concerns.

A. This Court Already Weighs The Effect Of A Second Federal Question As Part Of Its Policies On Finality.

This Court's decisions recognize that some federal issues are so severable or so important that this Court will review a state court decision on them, even though further pending state proceedings involve other federal questions.

In *Hudson Distributors, Inc. v. Eli Lilly & Co.,* 377 U.S. 386 (1964), a case decided prior to *Cox* but described therein as one of the fourth *Cox* "genre," (*Cox,* 420 U.S. at 484 n.11) appellant challenged the constitutionality of the Ohio fair trade law as conflicting with federal antitrust law. Justice Harlan in his dissent pointed out two additional federal questions which would have to be decided on remand to the Ohio Court of Common Pleas (the validity of a contract under the Sherman Antitrust Act and a possible conflict with another decision of this Court) and which might very well return to this Court. 377 U.S. at 386. Nevertheless, this Court reviewed the decision of the Ohio Supreme Court on the initial federal question.[5]

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[5] The type of federal question which *would* bar review is described by this Court in *Cox,* 420 U.S. at 478 n.6, namely eminent domain cases where both the federal question of taking and the federal question of just compensation must be decided in disposing of the constitutional issue.

This Court's decision in *Flynt* illustrates the weight which this Court gives to the competing considerations of a second federal question and an important federal policy. In *Flynt,* after stating that other federal issues would appear to be involved, this Court *nevertheless* considered whether the Ohio judgment denying the pre-trial motion to dismiss on the ground of insufficient evidence might fall within the fourth *Cox* category. In its analysis under this *Cox* test this Court looked only to whether a favorable decision for the petitioners might end the litigation and whether delaying review until conviction would seriously erode federal policy within the meaning of the prior cases.[6]

In this case, there are identifiable and important constitutional policies which are clearly being undermined by the decision of the California Supreme Court.[7] These have implications well beyond the litigants in this case and warrant immediate review.

B. Petitioner Meets The Fourth *Cox* Category.

The *Cox* categories are not as rigid as Respondent contends. *See Cox,* 420 U.S. at 477 ("*at least* four categories"). In any event, Petitioner meets the fourth of such categories. In the alternative, Petitioner meets the second (see subpart C hereafter).

Thus, although there are two federal questions, they are so intertwined as to be integral. *Compare San Diego Gas & Electric Co. v. City of San Diego,* 450 U.S. 621 (1981) *with First English Evangelical Lutheran Church v. County of Los Angeles,* 482 U.S. 304 (1987).

[6] The Court found no identifiable federal statutory or constitutional policy. The equal protection claim of selective prosecution, even though involving obscenity, was no different than any other selective prosecution claim reviewable after conviction and no federal policy barred a trial on dissemination of obscenity.

[7] Respondent contends that the only federal questions found sufficiently important under the *Cox* categories are First Amendment issues or procedural matters. *But see Hudson Distributors,* 377 U.S. 386 (involving antitrust issues) and *Goodyear Atomic Corporation v. Miller,* 486 U.S. 174 (1988) (federal preemption of state regulation of nuclear facilities).

Respondent contends that, if Petitioner prevails on due process grounds, the foreign commerce issue will be moot.[8] If so, Petitioner meets the fourth *Cox* test: (1) the litigation will end if petitioner prevails in this Court, (2) petitioner may prevail below on the merits on other grounds, thus rendering unnecessary review of the issue by this Court and (3) a refusal immediately to review the state court decision might seriously erode federal policy.

Respondent's chief argument is that the decision below on which the Petitioner might prevail must be a nonfederal ground. As *Flynt* shows[9] the fourth *Cox* test has not been interpreted so narrowly. In that test the erosion of federal policy constitutes "sufficient justification for immediate review" (*Cox*, 420 U.S. at 479), even if review could otherwise be avoided because of mootness.

Failure to review here will seriously erode important constitutional policies.

The Constitution allocates to the federal government the power to conduct foreign policy. Although Congress has ultimate authority to regulate commerce, in the absence of congressional regulation the policies of the dormant commerce clause prevail. *Hughes v. Oklahoma*, 441 U.S. 322, 325-26 (1979). The policy of uniformity presumptively prevails when Congress remains silent. *Wardair*, 477 U.S. at 7. Respondent does not deny that there is an accepted uniform standard to divide income among nations for tax purposes and that the California methodology is incompatible with and in conflict with that standard.

Like jurisprudence in the area of the First Amendment, these principles are well-established. However, the decision of the court below, admittedly based on the assumption that the reach of the

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[8] Petitioner does not concede that its foreign commerce causes will be moot if it were to prevail on due process grounds. The matter is not free from doubt however, and it is clear that Respondent would raise such procedural hurdle should Petitioner prevail.

[9] Respondent apparently agrees: Respondent states that in *Flynt* the petitioner met the first two conditions of the fourth *Cox* test even with the likelihood of additional federal questions. R.B. at 14. *See also Hudson Distributors*, 377 U.S. 386.

dormant commerce clause has been limited, erodes these principles.

This Court has affirmed, both before and after *Wardair*, that Congress must speak explicitly and affirmatively to remove state taxes from the scrutiny of the dormant commerce clause. The self-executing nature of the dormant commerce clause, creating a zone of free trade, is undercut by removing the check of explicit congressional action. This also affects the role of the federal executive in foreign policy.

Respondent argues that delay will not harm Petitioner. However, the policies at stake here do not affect just Petitioner or just other taxpayers.[10] Delay, or even worse, failure to review, will result in exactly the harm which these constitutional policies are meant to prevent.

There is urgency. Various governments, including the United States, could be patient while this case proceeded through the state courts: the lower California courts were following this Court's guidelines which take into account the sensitive nature of foreign relations.

But, in May, the California Supreme Court told the international community: (i) it had found an "interpretive framework" for a species of governmental silence that foreclosed resort to a dormant foreign commerce clause analysis, (ii) unswerving opposition to the use of worldwide combined reporting, through the five United States administrations—both Democrat and Republican—which have faced this issue, were nothing more than mere "executive aspirations", and (iii) California's retreat from use of worldwide combined reporting was a mere "meliorative" measure designed to "pacify critics."

Now twenty of the United States' main trading partners, which account for more than half of U.S. trade, tell this Court that they are "anxious" to have the constitutionality of the tax resolved before more harm is done to their relations with the United States. The United Kingdom told the United States government

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[10] However, it is clear that individuals are also entitled to the benefits of commerce clause protection. *Dennis v. Higgins*, ___ U.S. ___, 111 S. Ct. 865 (1991).

that the retaliatory legislation was not a mere ornament on the statute book and that immediate review of the California Supreme Court decision was "essential" to avoid an outcome that could risk damaging relations between these nations (Appendix A to United Kingdom Amicus Brief). Amici Curiae National Foreign Trade Council, Inc., et al., state that review is urgently needed to: "stave off a potentially destructive cycle of international retaliation that would interfere with foreign trade, disrupt international flows of capital and technology, and harm U.S. commercial interests abroad." National Foreign Trade Council Amicus Brief at 4.

The decision of the California Supreme Court, if left unreviewed, is as chilling in its own way on constitutional rights as was the decision of the Georgia Supreme Court in *Cox*. The California decision, left unreviewed, could effectively destroy protections accorded free trade by the dormant commerce clause. The decision has already cast a shadow on the ability of our Nation to conduct its foreign policy. Immediate review is essential to prevent erosion of these important constitutional rights.

C. In The Alternative, Petitioner Meets The Second *Cox* Category.

In the second *Cox* category ("the federal issue, finally decided by the highest court in the State, will survive and require decision regardless of the outcome of future state-court proceedings", *Cox*, 420 U.S. at 480) the key is not the absence of a second federal question. Rather the remaining questions, either state or federal, must be "wholly unrelated to the federal question" on which petitioner seeks review. *Id.* at 478.

This Court confirmed that severability of the remaining issues was the essential element of the second *Cox* test in *First English Evangelical Lutheran Church v. County of Los Angeles*, 482 U.S. 304 (1987). That case involved a claim that a prohibition on compensation for regulatory "takings" was unconstitutional. The California courts had assumed that a taking had occurred. This Court characterized *First English* as falling within the second *Cox* category, 482 U.S. at 310 n.3, and granted review because the

California court's assumption "isolate[d] the remedial question for our consideration." *Id.* at 311.[11]

Radio Station WOW v. Johnson, 326 U.S. 120 (1945), cited in *Cox* as an example of the second category, also demonstrates the rule of severability. The *WOW* Court, after noting that "[c]onsiderations of English usage as well as those of judicial policy" would justify a strict rule precluding review where any question remained, concluded that history did not support such a mechanical rule. 326 U.S. at 124-25. In particular, the mechanical rule was not applied where one part of a case is so "dissociated" from another that it is "[i]n effect . . . a multiple litigation allowing review of the adjudication which is concluded because it is independent of, and unaffected by, another litigation with which it happens to be entangled." *Id.* at 126.

The foreign commerce clause issues presented here are independent of the due process issue involving Respondent's regulations. Respondent might be able to fix its regulations, but the foreign commerce questions in the application of worldwide combined reporting would still remain.[12]

II

OTHER POLICY CONCERNS ARE BETTER SERVED BY IMMEDIATE REVIEW THAN BY DELAY

Respondent admits that a decision by this Court in favor of Petitioner on the foreign commerce grounds will end the litigation. This advances the policy concerns over waste. In *Mills v. Alabama,* 384 U.S. 214 (1966) this Court used, as an example of waste, expenditure of further time and energy in the state judicial

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[11] In describing the second *Cox* category, this Court did not list the absence of a second federal question as a requirement. In fact, later litigation did involve substantial federal questions. *See First English Evangelical Lutheran Church v. County of Los Angeles,* 210 Cal. App. 3d 1353 (1989).

[12] The Court of Appeal determined that the due process issue was not necessary to its decision on the foreign commerce clause matters and the California Supreme Court on remand expressly directed the California Court of Appeal to consider the due process issue free of the dormant commerce clause. Appendix B at 36-37; Appendix A at 49-50.

system already troubled by delays due to congested dockets. This case has been in the California court system for eight years, five of them in the appellate system.[13]

There is no interference with the California courts on the issue if this Court grants review. Any concerns of comity have already been met. Petitioner has subjected itself to the California state courts and the highest court of the state in that system has finally decided the issue which Petitioner now seeks to place before this Court.[14]

CONCLUSION

The patience of the international community should not be tested further. This Court should grant review and decide the important foreign commerce issues presented by this case.

Respectfully submitted,

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[13] Respondent's reference to two other cases (there are approximately 30 in the California court system all dependent upon this case on this issue) underscores the waste of judicial resources if this petition is denied. See also Appendix G.

[14] Respondent somewhat ambiguously states that a judgment in favor of the taxpayers on the due process issue would "render moot the Foreign Commerce Clause Issue *and holding* as to this case. . . ." R.B. at 8. Any decision of the Court of Appeal or the California Supreme Court in favor of or against Petitioner on the due process issue will not vacate the decision of the California Supreme Court already rendered. That decision is final, is precedent in California, and is already being applied.